

CAUSE NO. C-0181-13-B

WESLACO HEALTH FACILITIES	§	IN THE DISTRICT COURT
DEVELOPMENT CORPORATION,	§	
	§	
AND	§	
	§	
CITY OF WESLACO ,	§	
PLAINTIFFS,	§	93 RD JUDICIAL DISTRICT
VS.	§	
	§	
KNAPP MEDICAL CENTER; JAMES A.	§	
SUMMERSETT, III, JOHN L. LACKEY,	§	
RUDY SALINAS, ANABELL C.	§	
CARDONA, BRIAN A. HUMPHREYS,	§	
JR., NORMA I. MONTALVO, BERTHA	§	
SUAREZ AND ABRAHAM TANUS,	§	
IN THEIR OFFICIAL CAPACITIES AS	§	
MEMBERS AND ON BEHALF OF THE	§	
KNAPP MEDICAL CENTER BOARD	§	
OF DIRECTORS; KNAPP MEDICAL	§	
CENTER FOUNDATION, INC.; KNAPP	§	
COMMUNITY CARE FOUNDATION,	§	
INC.; PRIME HEALTHCARE	§	
FOUNDATION; AND	§	
PRIME HEALTHCARE SERVICES,	§	
DEFENDANTS.	§	
	§	
	§	
	§	HIDALGO COUNTY, TEXAS

**PLAINTIFFS' SUPPLEMENTAL REPLY TO DEFENDANTS' RESPONSE TO
PLAINTIFFS' MOTION TO COMPEL AND TO LIFT PROTECTIVE ORDER**

Plaintiffs, WESLACO HEALTH FACILITIES DEVELOPMENT CORPORATION and CITY OF WESLACO, file this their Supplemental Reply to Defendants' Response to Plaintiffs' Motion to Compel and To Lift the Protective Order and would respectfully show unto the Court the following:

I.
Hearing Background

Plaintiffs previously filed their Motion to Compel with this Court set for hearing on June 4, 2014. On that date, the Court granted Plaintiffs' Request for Production but subject to the Protective Order urged by Defendants, permitting Plaintiffs an opportunity to more thoroughly peruse the documents produced, and set a hearing for argument to lift the entire Protective Order in place for June 25, 2014. In support of this argument, Plaintiffs fully incorporate herein by reference their prior Motion and Reply and law thereto and supplements same as follows:

II.
**KNAPP MEDICAL CENTER is a public concern and the public
has the right to know what has been taken from them.**

1. KNAPP MEDICAL CENTER is a not-for-profit, acute care hospital with hospital facilities located at 108 E. 8th Street in Weslaco, Hidalgo County, Texas ("Hospital Property"). KNAPP MEDICAL provides medical and emergency services to residents and patients of the Rio Grande Valley with 233 private hospital rooms. Approximately seventy-five percent (75%) of the patients who seek health and emergency care from KNAPP MEDICAL CENTER do so through federal Medicaid or Medicare health programs. As such, KNAPP MEDICAL CENTER has historically provided an important source of healthcare to those Rio Grande Valley residents with low incomes and resources. *See* Important Message from the Board of Directors of KNAPP MEDICAL CENTER (Dec. 2011), *see* Exhibit "2" already on file among the Court's documents in this matter and incorporated by reference.

2. Plaintiff FACILITIES DEVELOPMENT CORPORATION, as a public instrumentality authorized to act on behalf of the CITY OF WESLACO, Texas, and the Plaintiff City itself, are vested with the responsibility to promote and develop new,

expanded or improved health facilities that assist the maintenance of the public health and public welfare pursuant to its Articles of Incorporation and By-Laws. *See, e.g.* Exhibit “1” to Plaintiff’s Original Petition. The terms and restrictive covenants mandated in the Special Warranty Deed dated December 17, 1987 from the Weslaco Hospital Authority to KNAPP MEDICAL CENTER have accrued to the CITY OF WESLACO by transfer of such assets and liabilities on or about January 18, 2013. These covenants constitute valid and valued property and contractual rights which serve Plaintiff’s constituents and permits Plaintiff to comply with its organizational purpose in addition to its purpose as a public instrumentality which is fully authorized to act on behalf of the CITY OF WESLACO, Texas.

3. The hospital property has been conveyed to a for-profit entity ostensibly through its alleged not-for-profit alter ego in violation of the restrictive covenants in detriment to the citizens of Weslaco and loss of contractual and property rights are accrued to these Plaintiffs.

As defined by the Texas Municipal League Legal Services,

Cities are formed for the purpose of managing the needs of people who live and work in close quarters. Cities provide basic services, such as streets, law enforcement, and utilities, as well as enact and enforce ordinances to protect the citizens of the community and foster a better living environment. City government in Texas, as in most of the United States, was founded on, and continues to evolve from, the premise that local communities know best how to run their local affairs.

See, e.g., http://www.tml.org/legal_pdf/TopLegalQuestions.pdf.

4. If this community is kept in the dark with regard the propriety and welfare of the sale of its principal medical provider, how can it possibly oversee and evaluate this life-and-death-impacting transaction?

III.

The Protective Order jeopardizes transparency of government and trust of the citizens it serves.

(a)History of KNAPP MEDICAL CENTER

5. In the mid-1950s, Weslaco citizens indicated in a Chamber of Commerce survey that they wanted a hospital to serve the Mid-Valley. The Mid Valley Hospital Development Corporation was formed after the McAllen District of the United Methodist Church agreed to run the hospital if a structure was built. Volunteers from Donna, Mercedes, Edcouch-Elsa, Progreso, and Weslaco went to work to raise money.

6. The KNAPP Foundation donated the first major gift of \$300,000. Volunteers raised another \$500,000 from among Mid Valley communities as donations from migrant workers, residents and local businesses. This \$800,000 was matched by a federal Hill-Burton grant to make the hospital a reality. *See*, <http://www.KNAPPmed.org/About-Us/History.aspx>.

7. The CITY OF WESLACO has provided support for KNAPP Hospital's mission and the constituents it serves since the hospital opened: creating the Hospital Authority¹, securing bonds, creating the Hospital Facilities Development Corporation and providing for capital improvements and expansion.² *Id.* However, despite their front-row participation in KNAPP's history, financing and success, these Plaintiffs find themselves prohibited from disclosing to these citizens information regarding the transfer of a hospital which they

¹ The CITY OF WESLACO created the Weslaco Hospital Authority (the "Authority") pursuant to the Hospital Authority Act for the purpose of administering the hospital, amongst other things, in the CITY OF WESLACO, Hidalgo County, Texas.

² The City, by authority granted by statute, created by Plaintiffs, the Corporation, with the power to provide, expand, and improve health facilities that the Corporation determines are needed to improve the adequacy, cost, and accessibility of health care, research and education. *See* HEALTH & SAFETY CODE § 221.002(a). The Corporation has the authority to issue bonds on behalf of the City for the purposes of Section 103, Internal Revenue Code of 1986 (26 U.S.C. Section 103). *Id.* § 221.002(b). The Corporation issued bonds in favor of Defendant, KNAPP MEDICAL CENTER, for the purpose of financing and refinancing the cost of acquiring, constructing and improving certain health care facilities.

themselves created and paid for.

(b) The fundamental differences between for-profit and not-for-profit entities as to mission and constituents demand disclosure.

8.

As opposed to a for-profit business created for the financial benefit of its owners and/or shareholders, a nonprofit entity has a mission that benefits the "greater good" of the community, society, or the world. It does not pay taxes, but it also cannot use its funds for anything other than the mission for which it was formed. Nonprofit organizations can and do make a profit, but it must be used solely for the operation of the organization or, in the case of a foundation, granted to other nonprofit organizations. The public sector-federal, state, county, and city government agencies-by definition serves the public good. Through taxation, public money ensures that programs and laws are put into place for all citizens to enjoy their rights without impinging on or impairing the rights of others. While public money benefits the public good, the public sector relies on nonprofits to provide the services and programs beyond its capabilities.

Bussey, Meg, *The Idealist Guide to Nonprofit Careers for First-time Job Seekers* at 21-23.

9. Public funds have paid for this hospital for the public good. The protective order intentionally denies the very public the hospital was intended to serve information as to who, what, where and how it was transferred to an out-of-state entity whose managerial arm has been accused of, among other things, recovering higher-than-average profits at the cost of patient care, canceling insurance contracts, suspending services, failing to meet minimum federal safety standards (which placed their Medicare funding at risk), upcoding patient diagnosis and treatment, transferring high numbers of patients from its emergency room to its hospital beds (specifically with patients on Medicare) and orchestrating a campaign of admitting Medicare patients- moving them from the emergency room to a hospital bed – in the interest of changing the fortune of a money-losing hospital. See, e.g., http://thomsonreuters.com/content/press_room/healthcare/tr_announces_top_health_syste

ms; Daniel Costello, Hospital group rejects system and cashes in, Los Angeles Times, July 8, 2007.

10. Prior to PRIME's acquisition, the KNAPP MEDICAL CENTER Mission Statement provided, "...the public purpose of KNAPP MEDICAL CENTER is to provide care to patients without financial means to pay for hospital services. Charity care will be provided to all patients who present themselves for care at KNAPP MEDICAL CENTER without regard to race, creed, color, or national origin and who are classified as financially or medically indigent." *See*, Exhibit Texas Nonprofit hospitals, Submitted Form Part II, Summary of Current Hospital Charity Care Policy and Community Benefits for Inclusion in DSHS Charity Care Manual as Required by Texas Health and Safety Code, § 311.0461-2011. *See*, Exhibit "A", attached hereto and incorporated by reference herein.

11. PRIME Healthcare Foundation founder and President Prem Reddy said in a news release, "The PRIME Healthcare Foundation will continue the mission of KNAPP MEDICAL CENTER and help it become one of the best hospitals in the state and nation." http://www.brownsvilleherald.com/news/local/article_94efdad2-5558-11e2-b640-0019bb30f31a.html. However, in stark contrast to the aforescribed historical KNAPP MEDICAL CENTER Mission Statement, KNAPP has now adopted the PRIME Mission Statement, *to wit*: "KNAPP MEDICAL CENTER endeavors to provide comprehensive, quality healthcare in a convenient, compassionate and cost effective manner." <http://www.KNAPPmed.org/About-Us/Mission-Statement.aspx>. Certainly, the Weslaco public and its surrounding communities have the right to know how their hospital and the mission proscribed therefore, has changed.

IV.

Affirmative efforts to hide information from the public is a pattern and practice of PRIME transactions, even in the sale of KNAPP.

12. Plaintiff's Motion to Compel documents a nearly year-long effort to review the transaction documents between PRIME and KNAPP. *See, id.* at page 4. Every purchase transaction in every state reviewed is likewise burdened with restricting disclosure of PRIME hospital asset acquisitions. For example, in 2013, Saint Clare's Health System (SCHS) and Catholic Health Initiatives (CHI) of Michigan signed an asset purchase agreement with PRIME Healthcare Services. Details of the asset purchase agreement were subject to a confidentiality agreement. *See, <http://www.PRIMEhealthcare.com/Press-Center/News/2013/Saint-Clare-s-Health-System-and-Catholic-Health-.aspx>*. The February 2013 PRIME Healthcare Agreement to purchase Saint Michael's Hospital in New Jersey likewise demanded confidentiality ("Terms of the deal were not disclosed..."). *See, <http://www.beckershospitalreview.com/hospital-transactions-and-valuation/PRIME-healthcare-signs-agreement-to-purchase-saint-michaels-in-nj.html>*. The attorney General of Rhode Island took action and mandated transparency of the intended confidentiality of the asset transfer agreement of October 2013 for the sale of the assets of Landmark medical Center and the Rehabilitation Center of Rhode Island to PRIME. *See, <http://www.riag.ri.gov/documents/healthcare/PRIMELandmarkFinalDecision.pdf>*. Opposition to the Acquisition of Providence and St. John's Hospitals in Kansas to PRIME in March 2013 demanded Attorney General Derek Schmidt scrutinize all sale details for clarity. ["Make sure everyone is crystal clear about all the terms of the agreement," Brenda Sharpe, chief executive of the REACH Healthcare Foundation, said.] As a result, Kansas Attorney General Schmidt announced that his office would keep the transaction record open to the public to receive additional comments about the sale.

See, <http://medcitynews.com/2013/03/californias-PRIME-healthcare-on-verge-of-purchasing-kansas-hospitals/#ixzz35T6y5TqJ>.

13. As to the KNAPP transaction itself, the confidential documents produced subject to the protective order speak to the breadth of intended non-disclosure of terms (*see*, paragraph 17, page 6 of the PRIME Letter of Intent (KMC Exhibit 13)) and thereafter successfully executed as revealed in KNAPP MEDICAL CENTER's Board of Directors' Minutes of November 20, 2012 (KMC Exhibit 21), noting the transaction would close by December 28, 2012 and, "Following closing...a public announcement will be made." *Id.* Indeed, that announcement was made on January 2, 2013, after the deed was done, a date intentionally selected and intended to obfuscate public scrutiny. *See*, http://www.themonitor.com/news/local/article_47429c6e-554b-11e2-ad30-001a4bcf6878.html. Those terms remain sealed, to date, from a public hungry to know what happened to their hospital.

V.

The Protective Order in place should be lifted as it requires Plaintiffs to be the gatekeepers of knowledge that rightfully belongs to people.

14. Plaintiffs bring this suit in the name of and on behalf of the citizens of Weslaco. It is anathema for these Plaintiffs to have received the benefit of this information and not provide it to its constituents who are thus specifically affected. Plaintiffs should not be forced to parse which documents it will disclose to the public; hence, its objection to the entire protective order. Based on the foregoing, the public need for the disclosure of the terms of this transaction and supporting documents far outweigh any specious claims of a need for protection.

VI.

Defenses of confidentiality and trade secrets asserted are inapplicable

15. Defendants have asserted that the documents produced are confidential and protected trade secrets yet fail to disclose how either of these defenses apply. *See*, Defendants Response to Plaintiffs’ Motion to Compel at Page 2. The documents without exception contain inescapably core public information as defined under Section 552.022 (a) of the Texas Public Information Act.

16. Further, Texas adopted the Uniform Trade Secrets Act, effective September 1, 2013. S.B. 953, 83rd Leg., Reg. Sess., § 4 (Tex. 2013) (the “Act”) which defines *trade secret*:

[I]nformation, including a formula, pattern, compilation, program, device, method, technique, process, financial data, or list of actual or potential customers or suppliers that (A) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use; and (B) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

TEX. CIV. PRAC. & REM. CODE § 134A.002(6).

17. Defendants have provided no guidance to the public nor this Court as to how the terms of this purportedly “**not-for-profit**” transaction have economic value that impacts Defendants’ competitive edge. What trade secrets are Defendants attempting to protect as it traverses the United States buying up purportedly “distressed and independent hospitals with limited scale and turning them around” when there are few **if any** competitors challenging their bids? *See*, KMC 634, Exhibit 2, *id*.

VII.

Defendants’ own actions have waived any alleged right to secrecy.

18. Defendants own actions have opened the door for complete disclosure of the documents to the public. While Defendants assert in their Response that “price” is a basis for

asserting “trade secret,” the Defendants themselves went forward with a press release dated March 18, 2013 (“Important News from KNAPP MEDICAL CENTER”) which not only discusses pricing but makes additional misleading or incomplete statements to the public which deception invites scrutiny and demands correction. *See*, Exhibit, “B” attached hereto and incorporated by reference herein. Among the “actual facts” the article sets forth:

- The article was presented because the CITY OF WESLACO joined this lawsuit alleging that the PRIME Healthcare Foundation not-for-profit (the 100% controlling member of KNAPP MEDICAL CENTER) after the Sale was an alter ego/sham corporation for the for-profit PRIME Healthcare Systems Organization, disclosed that Prem Reddy “founded and funded” the foundation but not that the funds came from the “for-profit,” that the “for profit” runs the “not-for-profit” arm, that Prem Reddy is the Chairman of the Board of PRIME’s for-profit, as well as every single nonprofit entity and that, until 2011, Reddy was the sole director of PHSF. (There are now five directors at PHSF including Reddy, his daughter Kavitha Bhatia, a former PHSI hospital director and two other associates). Prem Reddy is the Chairman of the Board of PRIME’s for-profit, as well as every single nonprofit entity. Until 2011 Reddy was the sole director of PHSF. There are now five directors at PHSF including Reddy, his daughter Kavitha Bhatia, a former PHSI hospital director and two other associates. Members of PHSF’s nonprofit hospital boards include family members, business associates, and others with a vested interest in PHSI. *See*, Exhibit “C”, attached to Plaintiffs’ Reply to Defendants’ Response to Plaintiffs’ Motion to Compel.³
- That despite the above, “PRIME Healthcare Foundation is governed by an independent board of directors which includes two elected city councilmen and a business executive who serves on the Board of Directors of the world famous Boys Town organization.” *Id.*
- That the January 1, 2013, PRIME Healthcare Foundation Membership Transfer transaction was a \$200 Million transaction (*see below* as to actual numbers).
- KNAPP MEDICAL CENTER remains a non-profit hospital and health care delivery system rendering hospital and healthcare services through KNAPP MEDICAL CENTER,

³ The Restated Certification of Formation of KNAPP MEDICAL CENTER, signed by KNAPP Board of Directors President John Lackey on December 21, 2012 and filed with the Texas Secretary of State discloses the same 5 individuals, all giving the address of 3300 E. Guasti Road, Suite 300, Ontario, California (same address as the for-profit PRIME HEALTHCARE SERVICES) as the current (and only) members of the Board of Directors of KNAPP MEDICAL CENTER.

KNAPP Surgery Center, and KNAPP Medical Group with charity care policies which are the same as those historically provided by KNAPP MEDICAL CENTER so as to ensure access to healthcare to those residents of the Rio Grande Valley with low income and/or resources....(*albeit* PRIME may sell KNAPP to another not-for-profit or for-profit hospital and drop its name after the expiration of certain specified terms. *See, e.g.*, KMC 53, Exhibit Membership Transfer Agreement).

- That the new “KCCF” received more than \$100 Million to support its mission of improving access to healthcare for low income, uninsured or medically underserved populations... (of which more than \$80 million came from KNAPP MEDICAL CENTER itself, not PRIME. *See, e.g.*, KMC 18, Exhibit 2, Membership Transfer Agreement; KMC 866, Exhibit, KNAPP MEDICAL CENTER’s Board of Directors’ Minutes of November 20, 2012).
- That the \$100 Million received by KCCF has and will include payments of approximately \$23 Million from the PRIME Healthcare Foundation and a transfer of more than \$80 Million in investments from KNAPP MEDICAL CENTER to KCCF (that is, PRIME acquired KMC, an entity valued at more than \$167 million, for approximately \$23 million to be paid over time. *See, e.g.*, KMC 81, Exhibit 2).
- That no payments whatsoever were being made to any member of the KNAPP MEDICAL CENTER Board of Directors or the KCCF Board of Directors as part of the transaction (but not after the transaction) *See*, Exhibit “B”, attached hereto.
- That KCCF is governed by a Board of Directors which is separate and apart from KNAPP MEDICAL CENTER’s Board of Directors who are John Lackey, Brian Humphreys, Norma Montalvo, Rudy Salinas, Bertha Suarez and Abraham Tanus (false-KCCF is governed with the same former members (except to include the not-mentioned Anabel Cardona) of the KNAPP MEDICAL CENTER Board of Directors who endorsed the sale transaction to PRIME. KNAPP MEDICAL CENTER’s current Board of Directors are the same as PHSI as set forth in Section VII, Paragraph 18, herein. *See Id.*).

19. Even the Response to the Motion pending herein makes representations to this Court which are contradicted by the produced “confidential” documents, *to wit*:

This lawsuit arose as a result of a transaction between the non-profit entities KNAPP MEDICAL CENTER, KNAPP Community Care Foundation, Inc. and PHSI Foundation, Inc. The transaction resulted in PHSI Foundation, Inc. becoming the sole member of KNAPP MEDICAL CENTER. As part of the transaction, all of the assets previously owned by KNAPP MEDICAL CENTER continue to be owned by KNAPP MEDICAL CENTER; PHSI Foundation, Inc. did not acquire ownership of any of the hospital’s assets.

See, Defendants’ Response to Plaintiffs’ Motion to Compel at Page 2, Paragraph 1.

20. However, both the Membership Transfer Agreement and the Minutes of the KNAPP Board of Directors recite that PHSF “will become the 100% controlling member of KNAPP MEDICAL CENTER, including all equity or membership in interests in KNAPP Medical Group, KNAPP Surgery Center and the Mid-Valley Physicians Association. PHSF shall acquire KNAPP’s facilities and real estate, including the hospital, Medical Plaza, Surgery Center, Medical Arts, Medical Condos, Conference Center, Parking lots, Helipad, and two vacant lots.” *See, e.g.*, KMC 18, Exhibit 2, Membership Transfer Agreement; KMC 866, Exhibit, KNAPP MEDICAL CENTER’s Board of Directors’ Minutes of November 20, 2012).⁴

21. Defendants cannot have it both ways: tooting their horns to the public as to the limited information they want the public to know while hamstringing the plaintiffs from providing the complete, unadulterated and uncompromised story of the KNAPP sale to their citizens to allow those citizens to “run their own [community’s] affairs” and decide whether, as PRIME contends, the loss of their hospital, their largest charitable assets, was “in the public interest.” *See*, KMC 664, Exhibit 9.

VIII.

22. Accordingly, Plaintiffs, WESLACO HEALTH FACILITIES DEVELOPMENT CORPORATION and CITY OF WESLACO, seek relief from this Court to permit the further inspection and copying of the disclosed documents without the burden of protecting documents which the public is entitled to view and permit them to prosecute this matter to resolution.

⁴ It appears the *only* realty PHSF did not take in the transaction was a vacant lot on 8th street which has some platting issues.

PRAYER

WHEREFORE, PREMISES CONSIDERED, Plaintiffs, WESLACO HEALTH FACILITIES DEVELOPMENT CORPORATION and CITY OF WESLACO, pray that this Honorable Court grant relief as specified herein and for any and all such further relief to which these parties may show themselves justly entitled.

Respectfully submitted,

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By /s/ Mary J. Ibarra-Myers
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**ATTORNEYS FOR PLAINTIFF,
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DEVELOPMENT CORPORATION
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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the above and foregoing document has, on this the 24th day of June, 2014, been forwarded to the following Counsel of Record:

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